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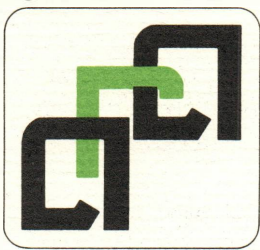
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Accounting Research Association

newsletter

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS, 666 FIFTH AVE., NEW YORK, N.Y. 10019

VOL. V, No. 10

December 13, 1972

ACCOUNTING FOR RETAIL LAND SALES COMPANIES

(The following statement has been issued by APB Chairman Philip L. DeFliese with the approval of the Board.)

"At the conclusion of an intensive four day meeting Saturday, December 9, the Accounting Principles Board of the American Institute of Certified Public Accountants announced that it had reached a conclusion by a substantial majority, to approve the AICPA land sales committee's position paper on accounting for retail land sales, after making many modifications in conjunction with the committee. The thrust of the modifications is to delay the recognition of sales and to reduce the profit reported in the first year as compared with earlier drafts. The action is subject to final drafting and balloting.

"The new draft will specify use of both accrual and installment accounting for retail land sales but will limit the use of an accrual method to only those situations where stringent criteria are met. Sales under either method will not be recognized until cash payments received aggregate ten percent of the contract price and the customer's cancellation privilege period has expired.

"The Board reaffirmed the position it took in APB Opinion No. 10 which permits use of the installment method only in cases when serious doubt of the collectibility of receivables exists. The SEC and Financial Analysts Federation both recommended use of the installment method in almost all cases involving typical sales in this industry.

"Use of the accrual method will be required on a project by project basis if the following criteria are met:

- (1) The properties clearly will be useful for residential or recreational purposes when the payment period is completed.
- (2) The company's financial capabilities assure its ability to fund or bond the planned improvements.
- (3) The project's planned improvements must have progressed beyond preliminary stages and there is evidence that the work will be completed according to plan.
- (4) Collection experience of the project or related projects indicates that collectibility of receivable balances is reasonably predictable and that ninety percent of the contracts in force six months after sales are recorded will be collected in full.

"Until such time as collection experience of a project warrants use of the accrual method, contracts must be accounted for on the installment method which permits deferment of related selling costs. Until such time as the contract payments aggregate ten percent of contract price and promised performance becomes predictable, payments will be treated as deposits. The new accrual method requires (1) deferment of a portion of the contract price to cover cost and profit applicable to future development work;

(continued)

(2) discount of contract receivables to yield an interest rate equal to the retail installment credit rate which is currently about 12 percent.

"In order to provide earnings trend comparability, the new position paper will require restatement of prior years' results of many companies and it is hoped that the paper will be issued in time for 1972 annual reports to be published using the new accounting concepts. It is expected that the text of the paper will be available January 1st.

"Reached by telephone, John C. Burton, chief accountant of the SEC, expressed disappointment but affirmed his position, subject to review of the final draft, that he would recommend the Commission's acceptance of the paper if a solid two thirds majority of the APB endorsed it. The New York Stock Exchange had previously indicated that it would accept a similar paper if cash flow data were required in the financial report. The draft contains such a requirement."

TWO PROPOSED OPINIONS APPROVED FOR EXPOSURE

Subject to drafting of specific language, two proposed Opinions should be released for exposure in January.

Disclosure of Lease Commitments by Lessees: Provides for separate disclosure of (a) the total lease rentals charged against operations for each period presented; (b) the minimum annual rentals payable in each of the five succeeding years and thereafter by five-year periods for all leases with a remaining noncancellable term of more than one year; and (c) the present value of all leases with more than a one-year remaining life, computed on a net basis, if reasonably determinable. Effective date will be for balance sheets issued on fiscal years ending December 31, 1973 and thereafter.

Nonmonetary Transactions: Provides that, in general, the accounting for exchanges of nonmonetary assets and for nonreciprocal transfers of assets either to or from the enterprise should be based on the fair values of assets involved.

However, this general principle of recording fair values is modified for some transactions in order to accommodate problems of measuring fair values or questions about recognizing revenue before the earning process is complete. Specifically, carrying values of assets should be used to record (1) an exchange or nonreciprocal transfer if fair values are not determinable; (2) an exchange involving inventory-type items; (3) an exchange of similar productive assets; (4) a distribution to owners in connection with a spin-off, other form of reorganization or liquidation, or a rescission of a prior business combination. The proposed Opinion will be applicable to transactions consummated after January 1, 1973.

Also, the previously approved exposure drafts on the proposed Opinions on Interim Financial Statements and Extraordinary Items should be available by the end of the month. (See ARA Newsletter, November 8, 1972.)

AUDIT GUIDES APPROVED

The APB chairman has approved audit guides on Stock Life Insurance Companies and Brokers and Dealers in Securities for publication in January.